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UNITED STATES DISTRICT COURT  
CENTRAL DISTRICT OF CALIFORNIA

In re DDi CORPORATION  
SECURITIES LITIGATION

This Document Relates To:  
ALL ACTIONS

THIS CONSTITUTES NOTICE OF ENTRY  
AS REQUIRED BY FRCP, RULE 77(d).

Master File No. CV 03-7063 NM  
(SJHx)

(Consolidated with Nos. CV 03-7883;  
CV 03-7999; CV 03-8344; CV 04-  
0735)

CLASS ACTION

OPINION & ORDER GRANTING IN  
PART AND DENYING IN PART  
DEFENDANTS' MOTIONS TO  
DISMISS THE SECOND AMENDED  
CONSOLIDATED CLASS ACTION  
COMPLAINT [119, 120, 123]

**I. INTRODUCTION**

This is a consolidated securities class action arising out of a February 14, 2001 secondary public offering of DDi Corporation ("DDi") common stock and convertible subordinated notes. On February 22, 2005, Plaintiffs filed a Second Amended Consolidated Class Action Complaint ("SAC") asserting claims under sections 11, 12(a)(2), and 15(a) of the Securities Act of 1933 against various persons and entities associated with DDi and/or this offering. Before the court are three motions to dismiss the SAC. For the reasons set forth below, these motions are GRANTED in part and DENIED in part.

## II. FACTUAL AND PROCEDURAL BACKGROUND

DDi specialized in creating prototype Printed Circuit Boards ("PCBs") on an expedited basis – often within 24 hours – for a premium price. SAC ¶¶ 5, 48-51. In addition to this "quick-turn prototyping," DDi provided "value-added services," including: (1) "[f]ast-track assembly services . . . for the attachment of materials to a small number of PCBs," and (2) "[p]re-production volume services . . . involv[ing] the generation and delivery of a small volume of units." *Id.* ¶¶ 5, 50. DDi's value-added services had a longer turnaround time and tended to return lower profit margins than its quick-turn prototyping. *Id.* ¶ 5.

On February 14, 2001, through a firm commitment underwriting, DDi and various shareholders issued 6 million shares of DDi common stock in a secondary public offering (the "Offering") that captured \$132 million in proceeds. *Id.* ¶ 2.<sup>1</sup> As part of the Offering, DDi also issued 5.25% convertible subordinated notes (the "Convertible Notes"), due March 1, 2008, which had an aggregate principal amount of \$100 million and generated \$97 million in proceeds. *Id.* The Offering was made pursuant to a Form S-1 Registration Statement filed with the Securities and Exchange Commission ("SEC") on January 31, 2001, and a prospectus filed with the SEC in February 2001 (collectively, the "Prospectus"). *Id.* ¶ 3.

Plaintiffs allege that the Prospectus "contained false and misleading statements of material fact and omitted to state material facts necessary to make the statements [made therein] not misleading." *Id.* ¶ 62. Plaintiffs contend that the Prospectus was false and misleading on at least six grounds.

First, Plaintiffs assert that the financial reports included in the Prospectus were false and misleading because they were inflated by "accounting

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<sup>1</sup> A firm commitment underwriting is one in which the underwriter agrees to buy all the shares to be issued and remains financially responsible for any securities not purchased. See *Shaw v. Digital Equip. Corp.*, 82 F.3d 1194, 1215 (1st Cir. 1996).

improprieties.” Id. ¶ 79. In particular, Plaintiffs allege that DDi, in violation of Generally Accepted Accounting Principles (“GAAP”) and its own internal accounting policies, “recognized revenue on (1) the premature shipment of orders to clients . . . prior to the authorized delivery date; and (2) the shipment of orders from one DDi facility to another.” Id. ¶ 80. See also id. ¶¶ 86-87.

Second, Plaintiffs allege that the Prospectus “misrepresented the amount of DDi customers and failed to disclose that DDi had lost many of its historically largest customers.” Id. ¶ 74. The Prospectus provided:

We currently have over 2,000 customers. Our largest original equipment manufacturer customers in terms of net sales are Alcatel, Ericsson, IBM, Intel and Marconi Communications. . . . We have achieved a net increase of approximately 200 customers since January 1, 2000, excluding increases resulting from acquisitions. . . . We announced that during the fourth quarter we added over 100 new customers to increase our diversified customer base to more than 2,000 original equipment manufacturers and other electronic manufacturing service providers. . . . We have been successful at retaining customers and have worked with our three largest customers since 1991.

Prospectus at 2, 3, 52.<sup>2</sup> See also SAC ¶ 68. Plaintiffs allege that in reality, DDi had 500 customers, and that “by the fourth quarter 2000, DDi was booking very little or no business from, *inter alia*, Alcatel, Redback, Intel, Marconi, 3Com, IBM, Nortel, and Cisco.” SAC ¶ 74.

Third, Plaintiffs allege that the Prospectus was false and misleading because it “misrepresented and omitted to disclose that by no later than the fourth quarter

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<sup>2</sup> The court takes judicial notice of this document. See Branch v. Tunnell, 14 F.3d 449, 454 (9th Cir. 1994) (citation omitted) (on Rule 12(b)(6) motion to dismiss, court may consider “documents whose contents are alleged in a complaint and whose authenticity no party questions, but which are not physically attached to the pleading”), overruled on other grounds by Galbraith v. County of Santa Clara, 307 F.3d 1119 (9th Cir. 2002).

1 of 2000, DDi's quick-turn and value-added business had suffered precipitous  
2 declines and DDi's transaction pipeline had dried up." Id. ¶ 75. While the  
3 Prospectus stated that DDi encountered "strong" demand in the fourth quarter of  
4 2000, that DDi's end-markets were "fast-growing," and that DDi was anticipating  
5 "near-term increases in customer demand," Plaintiffs allege that in reality, "the  
6 overall demand for quick-turn and value-added PCBs [had] dropped off  
7 precipitously," "customers [had been] sen[ding] value-added business overseas,"  
8 "[m]any of the customers . . . [had] tried to cancel [orders]," "many of DDi's  
9 customers [had] stopped doing business with [DDi]," "DDi's sales pipeline [had]  
10 dried up," and "DDi was forced to implement across the board employee pay  
11 cuts." Id. ¶¶ 56, 64, 65, 69, 77.

12 Fourth, Plaintiffs allege that the Prospectus "misrepresented and omitted to  
13 disclose that in 2000, DDi's revenues were as dependent on the high-premiums  
14 [that] DDi [was] reap[ing] from its value-added services . . . as . . . [they were on]  
15 its quick-turn business, and that by late-2000 DDi was not receiving high-  
16 premiums on its value-added services." Id. ¶ 76. According to Plaintiffs,  
17 "[b]efore 2000, DDi was focused primarily on quick-turn prototyping because the  
18 quick-turn work commanded large premiums due to the fast turn-around times,  
19 whereas higher volume value-added services yielded lower profit margins." Id.  
20 ¶ 53. However, "[s]tarting in 1999, . . . the overall demand for PCBs grew and  
21 industry capacity could not keep up." Id. ¶ 54. Consequently, "DDi customers  
22 increased their demand for volume orders of PCBs, paying quick-turn pricing for .  
23 . . value-added services." Id. As a result, "DDi turned its focus to and realized at  
24 least 50% of its revenues from its value-added services business." Id. Plaintiffs  
25 allege that "[t]he public was unaware of this change," id. ¶ 55, and that the  
26 Prospectus failed to reveal both that it had occurred and "that by late-2000 DDi  
27 was no[] [longer] receiving high-premiums on its value-added services." Id. ¶ 76.  
28

1 Fifth, Plaintiffs allege that the Prospectus was misleading in that it asserted  
 2 that DDi was intending to increase its manufacturing capacity. Id. ¶ 77. While the  
 3 Prospectus provided that DDi “ha[d] plans to expand both of [its] manufacturing  
 4 facilities in California, as well as those in Texas and the United Kingdom,”  
 5 Plaintiffs allege that these statements were “misleading and incomplete as DDi  
 6 experienced significant layoffs and actually reduced operations in early 2001.”  
 7 Prospectus at 3, 5; SAC ¶¶ 70, 77.<sup>3</sup>

8 Sixth, Plaintiffs allege that the Prospectus’s “outlook” was false and  
 9 misleading. SAC ¶ 78. The Prospectus provided:

10 Outlook. We announced on January 25, 2001 that, while  
 11 acknowledging recent macro-economic indicators suggesting an  
 12 economic slowdown, we remain comfortable with our performance  
 13 estimates for 2001. Unlike many volume printed circuit board  
 14 manufacturers, we specialize in providing prototype and low-quantity  
 15 manufacturing services for research and development programs and  
 16 new product development, with production lead times that can be as  
 17 short as 24 hours. We believe this focus provides higher margins and  
 18 lower performance volatility by insulating us from large order  
 19 cancellation or deferment decisions made in light of softening market  
 20 forecasts. We believe that our large and diverse customer base also  
 21 makes us less vulnerable to individual customer shifts in demand.  
 22 We announced that for 2001 we are targeting increases in net sales

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23 <sup>3</sup> Plaintiffs also allege that the Prospectus “stated that [DDi] had sufficient  
 24 business to maximize its burgeoning facility space.” SAC ¶ 70. However, the identified  
 25 portion of the Prospectus does not make this assertion. See Prospectus at 54  
 26 (“Accomplishing [our] operations in time-critical situations, as we do, required the  
 27 attention of highly-qualified personnel. Furthermore, our manufacturing systems are  
 28 managed to maximize flexibility to accommodate widely varying projects for different  
 customers with minimal or no turnover time. We seek to maximize the use of our  
 production and manufacturing capacity through the efficient management of time-critical  
 production schedules. We conduct our operations in several buildings that we own or  
 lease. We believe our facilities are currently adequate for our operating needs.”).

1 and earnings per share in excess of 25% over our 2000 results. A  
 2 number of factors, including those described below in "Risk Factors,"  
 3 will affect our ability to achieve these goals, and there can be no  
 4 assurance that we will do so.

5 Prospectus at 4.<sup>4</sup> Plaintiffs allege that this "glowing outlook was untenable and  
 6

7 <sup>4</sup> The Prospectus contained the following "Risk Factors":

- 8 • This offering involves a high degree of risk. . . . If any of the  
 9 following risks . . . actually occur, our business, financial condition  
 10 and operating results would likely suffer. In that event, the market  
 11 price of our stock could decline, and you could lose all or part of the  
 12 money you paid to buy our common stock.
- 13 • A downturn in the communications or networking equipment  
 14 industries would likely negatively impact our revenues.
- 15 • A majority of our customers are in the communications and  
 16 networking equipment industries, which are characterized by intense  
 17 competition, relatively short product life-cycles and significant  
 18 fluctuations in product demand. In addition, these industries are  
 19 generally subject to rapid technological change and product  
 20 obsolescence. Furthermore, these industries are subject to economic  
 21 cycles and have in the past experienced, and are likely in the future  
 22 to experience, recessionary periods. A recession or any other event  
 23 leading to excess capacity or a downturn in the communications or  
 24 networking equipment industries would likely negatively impact our  
 25 revenues.
- 26 • Our operating results have fluctuated in the past because we sell on a  
 27 purchase-order basis rather than pursuant to long-term contracts. We  
 28 are therefore sensitive to variability in demand by our customers. . . .  
 Because of these factors, you should not rely on quarter-to-quarter  
 comparisons of our results of operations as an indication of our  
 future performance.
- Because we depend on a core group of significant customers, our  
 (continued . . .)



1 incomplete as DDi had suffered a precipitous loss of both value-added and quick-  
 2 turn business leading up to the . . . Offering such that DDi's sales pipeline was  
 3 depleted entering 2001." SAC ¶ 78.

4 Plaintiffs assert that these various false and misleading statements and  
 5 omissions caused the "Offering of common stock and convertible notes [to be]  
 6 completed at artificially inflated prices." *Id.* ¶ 11. In fact, "[o]nce DDi's [true]  
 7 financial condition became apparent, the Company's stock price fell below \$1.00  
 8 per share." *Id.* ¶ 12. On August 20, 2003, DDi announced that it had filed for  
 9 reorganization under Chapter 11 of the United States Bankruptcy Code. *Id.* ¶ 4.

10 On October 1, 2003, the first complaint related to this action was filed.  
 11 After various other complaints were filed, the court consolidated the actions and  
 12 appointed Paul Poppe ("Poppe"), LeRoy Schneider ("Schneider"), and Rand  
 13 Skolmick ("Skolmick") as lead plaintiffs. On July 26, 2004, lead plaintiffs Poppe,  
 14 Schneider, and Skolmick, along with representative plaintiff Municipal  
 15 Employees' Retirement System of Louisiana ("MERSL"), filed a Consolidated  
 16 Amended Complaint ("CAC") on behalf of those who purchased DDi common  
 17 stock between December 19, 2000 and April 29, 2003, including those who  
 18 acquired DDi common stock in the Offering.<sup>5</sup> The CAC asserted that the above-  
 19 mentioned false and misleading statements and omissions in the Prospectus, as

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21 results of operations may be negatively impacted if key customers  
 22 discontinue the use of our services.

- 23 • As a result of our level of debt and the terms of our debt instruments  
 24 . . . our vulnerability to adverse general economic conditions is  
 25 heightened.

26 Prospectus at 9-14.

27 <sup>5</sup> The CAC did not assert claims on behalf of those who purchased the Convertible  
 28 Notes.

well as a series of other allegedly false and misleading statements issued by DDi between December 19, 2000 and April 29, 2002, were part of a carefully-crafted, fraudulent scheme to mislead investors. The CAC advanced causes of action under: (1) section 11 of the Securities Act of 1933 ("Securities Act"), (2) section 12(a)(2) of the Securities Act, (3) section 15(a) of the Securities Act, (4) section 10(b) of the Securities and Exchange Act of 1934 ("Exchange Act") and Rule 10b-5 promulgated thereunder, and (5) section 20(a) of the Exchange Act.

On January 7, 2005, the court issued an order dismissing the CAC. See In re DDi Corp. Sec. Litig. ("In re DDi"), 2005 U.S. Dist. LEXIS 1056 (C.D. Cal. Jan. 7, 2005). The court found that although Fed. R. Civ. P. 8(a)'s notice pleading model generally applied to Securities Act claims and Fed. R. Civ. P. 9(b)'s heightened pleading model applied to Exchange Act claims, Plaintiffs' entire CAC was "grounded in fraud," and, therefore, subject to the heightened pleading requirements imposed by Rule 9(b). Id. at \*57-61.<sup>6</sup> The court then found that the CAC failed to satisfy Rule 9(b) because it did not particularly allege that any of Defendants' statements were materially false and misleading. Id. at \*62-79.

On February 22, 2005, lead plaintiffs Poppe and Schneider, along with a new representative plaintiff, Robert Watson ("Watson"), filed the instant SAC.<sup>7</sup> The SAC, unlike the CAC, focuses solely on the Prospectus and asserts only Securities Act claims. Additionally, Plaintiffs now purport to assert claims on behalf of those who purchased DDi common stock pursuant to or traceable to the Prospectus, as well as on behalf of those who purchased the Convertible Notes. See SAC ¶ 42. Finally, the SAC, unlike the CAC, asserts that the alleged

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<sup>6</sup> Rule 9(b) provides that "[i]n all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity." Fed. R. Civ. P. 9(b).

<sup>7</sup> Despite Defendants' arguments to the contrary, the SAC does not assert any claims based upon allegations previously dismissed with prejudice.



misrepresentations and omissions in the Prospectus were the result of negligence, not fraud. See, e.g., id. ¶ 41 (“Each of the defendants owed to the purchasers of DDi stock and the Convertible Notes . . . the duty to make a reasonable and diligent investigation of the statements contained in the . . . Prospectus . . . . This duty included performing an appropriate investigation to ensure that the statements contained therein were true, and that there were no omissions of material fact required to be stated in order to make the statements contained in the . . . Prospectus not misleading. . . . [E]ach of the defendants violated these specific duties and obligations.”). See also id. ¶¶ 95-96, 113.

In the SAC, Plaintiffs assert claims under the Securities Act against three groups of defendants. First, they sue the following Individual Defendants: Charles Dimick, Chairman of the Board of Directors of DDi (“Dimick”); Bruce D. McMaster, President and Chief Executive Officer of DDi (“McMaster”); Joseph P. Gisch, Vice President and Chief Financial Officer of DDi (“Gisch”); Gregory Halvorson, Vice President of Operations of DDi (“Halvorson”); John Peters, Vice President of Sales and Marketing of DDi (“Peters”); and Mark R. Benham, a director of DDi from November 1998 to December 31, 2002 (“Benham”) (collectively, the “Individual Defendants”). Second, Plaintiffs name: Bain Capital, Inc., a shareholder of DDi (“Bain”); David Dominik, a director of DDi from November 1998 to December 31, 2002 and a managing director of Bain from 1990 until March 2000 (“Dominik”); Stephen G. Pagliuca, a director of DDi and a managing director of Bain (“Pagliuca”); Stephen M. Zide, a director of DDi and a principal at Bain (“Zide”); and Edward W. Conrad, a director of DDi and a principal at Bain (“Conrad”) (collectively, the “Bain Defendants”). Third, Plaintiffs name the following defendants for their role as underwriters in the Offering: Credit Suisse First Boston Corporation (“CSFB”); FleetBoston Financial Corporation (“Fleet”), the successor-in-interest to Robertson Stephens, Inc. (“Robertson”); J.P. Morgan Securities, Inc. (“JP Morgan”); and Needham &

1 Company, Inc. ("Needham") (collectively, the "Underwriter Defendants"). Id.  
2 ¶¶ 36-39.<sup>8</sup> DDi is not named as a defendant because it has filed a petition for  
3 reorganization under Chapter 11 of the United States Bankruptcy Code. Id. ¶ 21.  
4 The SAC asserts claims under sections 11, 12(a)(2), and 15(a) of the Securities  
5 Act.

6 On March 25, 2005, each of the three groups of defendants filed separate  
7 motions to dismiss the SAC pursuant to Rule 9(b) and Rule 12(b)(6) of the Federal  
8 Rules of Civil Procedure. On April 25, 2005, Plaintiffs filed one opposition to  
9 these three motions. On May 6, 2005, the Individual Defendants filed a  
10 supplemental brief in further support of their motion to dismiss. On May 20,  
11 2005, Plaintiffs filed an opposition to the Individual Defendants' supplemental  
12 brief.

### 13 14 **III. LEGAL STANDARD**

15 A court should dismiss a complaint under Rule 12(b)(6) of the Federal  
16 Rules of Civil Procedure for failure to state a claim only where it appears beyond  
17 doubt that plaintiff can prove no set of facts in support of the claim which would  
18 entitle the plaintiff to relief. Conley v. Gibson, 355 U.S. 41, 45-46 (1957). All  
19

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20  
21 <sup>8</sup> The Underwriter Defendants were the four lead underwriters in the Offering.  
22 SAC ¶¶ 36-39. Plaintiffs allege that CSFB sold and distributed 2,700,000 shares of DDi  
23 common stock and \$100 million worth of Convertible Notes in the Offering; that  
24 Robertson sold and distributed 1,462,500 shares of DDi common stock and \$100 million  
25 worth of Convertible Notes; that JP Morgan sold and distributed 1,462,500 shares of DDi  
26 common stock and \$100 million worth of Convertible Notes; and that Needham sold and  
27 distributed 375,000 shares of DDi common stock. Id.

28 Through the Underwriter Defendants, DDi sold 3 million shares, Bain sold  
2,296,503 shares, McMaster sold 82,500 shares, Dimick sold 82,500 shares, Gisch sold  
22,500 shares, Halvorson sold 22,500 shares, and Peters sold 45,000 shares. Id. ¶¶ 22-26,  
28, 60-61. McMaster, Dimick, Gisch, Dominik, Pagliuca, Zide, Conrad, and Benham  
signed the Prospectus. Id. ¶¶ 22-24, 30-34, 60.

1 allegations of material fact are taken as true and construed in the light most  
2 favorable to the nonmoving party. Smith v. Jackson, 84 F.3d 1213, 1217 (9th Cir.  
3 1996).

4 Review is generally limited to the contents of the complaint. Allarcom Pay  
5 Television, Ltd. v. Gen. Instrument Corp., 69 F.3d 381, 385 (9th Cir. 1995).

6 However, material that is properly presented to the court as part of the complaint  
7 may be considered as part of a motion to dismiss. Lee v. City of Los Angeles, 250  
8 F.3d 668, 688-89 (9th Cir. 2001). If a plaintiff fails to attach to the complaint the  
9 documents on which it is based, the defendant may attach those documents to a  
10 Rule 12(b)(6) motion to show that they do not support the plaintiff's claim. Id. In  
11 addition, the court may take judicial notice of facts that are capable of accurate  
12 and ready determination by resort to sources whose accuracy cannot be  
13 questioned. See Fed. R. Evid. 201.

#### 14 15 IV. ANALYSIS

16 Defendants attack Plaintiffs' three Securities Act claims collectively and  
17 individually. First, Defendants argue that Plaintiffs cannot assert any Securities  
18 Act claims on behalf of those who purchased the Convertible Notes because:  
19 (1) Plaintiffs lack standing to do so, and (2) such claims are time-barred. Second,  
20 Defendants contend that the SAC must be dismissed because it, like the CAC, fails  
21 to satisfy Rule 9(b)'s heightened pleading requirements for averments of fraud.  
22 Third, Defendants argue that Plaintiffs' § 11 claim must be dismissed because:  
23 (1) Plaintiffs have failed to allege the material falsity or misleading nature of any  
24 statement in the Prospectus, (2) the "negative causation" defense bars Plaintiffs'  
25 claim(s), and (3) the allegedly false and misleading statements in the Prospectus  
26 are rendered inactionable by the puffery doctrine, the bespeaks caution doctrine,  
27 and/or the safe harbor provision of the Private Securities Litigation Reform Act  
28 ("PSLRA"). Fourth, with respect to Plaintiffs' § 12(a)(2) claim, Defendants

1 argue: (1) that the entire claim must be dismissed because the Prospectus was not  
2 materially false and misleading, (2) that the claim must be dismissed insofar as it  
3 is asserted on behalf of those who purchased DDi common stock "traceable to" the  
4 Prospectus, (3) that the claim must be dismissed insofar as it is asserted against the  
5 Individual Defendants and Bain because they were not statutory "offerors" or  
6 "sellers" under § 12(a)(2), and (4) that the claim must be dismissed insofar as it is  
7 asserted against the Underwriter Defendants because Plaintiffs have failed to  
8 allege which particular underwriter sold them DDi common stock. Fifth,  
9 Defendants argue that Plaintiffs' § 15(a) claim must be dismissed insofar as it is  
10 asserted against Bain because Plaintiffs have failed to allege that Bain was a  
11 "controlling person."

12 **A. Claims Asserted on Behalf of Convertible Note Purchasers**

13 In the SAC, unlike in the CAC, Plaintiffs assert claims on behalf of those  
14 who purchased Convertible Notes. Defendants argue that Plaintiffs cannot assert  
15 these claims because: (1) they do not have standing to do so, and (2) the claims are  
16 barred by the statute of limitations.

17 **1. Standing**

18 The named plaintiffs purchased DDi common stock; they do not claim to  
19 have purchased Convertible Notes. See SAC ¶¶ 19-20. Consequently, Defendants  
20 argue that Plaintiffs lack standing to assert claims on behalf of those who did  
21 purchase Convertible Notes.

22 In In re MobileMedia Sec. Litig., 28 F. Supp. 2d 901 (D.N.J. 1998), the  
23 District Court of New Jersey encountered a similar situation. There, the court  
24 stated:

25 Defendants challenge[] the standing of stock purchasers to bring  
26 [Securities Act] claims on behalf of the purchasers of . . . Notes. . . .  
27 "That a suit may be a class action adds nothing to the question of  
28 standing, for even named plaintiffs who represent a class must allege

and show that they personally have been injured.” Lewis v. Casey, 518 U.S. 343, 357 (1996). In the instant matter, Plaintiffs have alleged an injury traceable to the Secondary Offering – the same offering in which the Notes were issued. Courts have allowed those with valid securities claims to represent the interests of the purchasers of other types of securities in class action suits. Given Plaintiffs have sufficiently alleged individual cognizable injuries pursuant to [the Securities Act], Plaintiffs have standing to bring these claims [on behalf of those who purchased the notes]. Concerns over whether stock purchasers should represent notes purchasers are better addressed at the time of class certification.

Id. at 911 n. 7 (selected citations omitted).

The court agrees with this analysis. Here, lead plaintiffs, Poppe and Schneider, and representative plaintiff, Watson, allege to have purchased DDi common stock from the Offering. Like the plaintiffs in In re MobileMedia, Plaintiffs assert claims not only on behalf of those who purchased stock from this offering, but also on behalf of those who purchased notes traceable to the Offering. “Given Plaintiffs have sufficiently alleged individual cognizable injuries pursuant to [the Securities Act], Plaintiffs have standing to bring these claims.” Id. Accordingly, the court denies Defendants’ motions insofar as they assert that Plaintiffs lack standing to assert claims on behalf of those who purchased Convertible Notes.

## 2. Statute of Limitations

Defendants argue that the statute of limitations bars Plaintiffs’ claims asserted on behalf of those who purchased the Convertible Notes. The statute of limitations for Securities Act claims is set forth in § 13, which provides that “[i]n no event shall any . . . action be brought to enforce a liability created under [section 11 or section 12(a)(1)] more than three years after the security was bona fide offered to the public, or under [section 12(a)(2)] more than three years after the sale.” 15 U.S.C. § 77m.

1 Here, Plaintiffs did not raise claims on behalf of the Convertible Note  
2 purchasers until February 22, 2005, when they filed the SAC. This was far more  
3 than 3 years after the February 2001 Offering. Consequently, absent some  
4 exception, Plaintiffs' claims are time-barred insofar as they are asserted on behalf  
5 of the Convertible Note purchasers.

6 Recognizing this fact, Plaintiffs argue that the Convertible Note purchasers'  
7 claims "relate back" under Rule 15(c) of the Federal Rules of Civil Procedure to  
8 the date that the "initial complaint" was filed in this action. See Opp. at 36. Rule  
9 15(c) provides:

10 An amendment of a pleading relates back to the date of the original  
11 pleading when . . . (2) the claim or defense asserted in the amended  
12 pleading arose out of the conduct, transaction, or occurrence set forth  
13 or attempted to be set forth in the original pleading, or (3) the  
14 amendment changes the party or the naming of the party against  
15 whom a claim is asserted if the foregoing provision (2) is satisfied  
16 and, within the period provided by Rule 4(m) for service of the  
17 summons and complaint, the party to be brought in by amendment  
18 (A) has received such notice of the institution of the action that the  
19 party will not be prejudiced in maintaining a defense on the merits,  
20 and (B) knew or should have known that, but for a mistake  
concerning the identity of the proper party, the action would have  
been brought against the party.

21 Fed. R. Civ. P. 15(c).

22 "The Advisory Committee Note to the 1966 Amendment to Rule 15(c)  
23 observes that '[t]he relation back of amendments changing *plaintiffs* is not  
24 expressly treated in revised Rule 15(c) since the problem is generally easier' and  
25 goes on to comment that 'the attitude taken in revised Rule 15(c) toward change of  
26 defendants extends by analogy to amendments changing plaintiffs.'" Immigrant  
27 Assistance Project of the Los Angeles County Fed'n of Labor v. Immigration and  
28 Naturalization Serv., 306 F.3d 842, 857 (9th Cir. 2002) (emphasis added) (quoting



1 Fed. R. Civ. P. 15(c) advisory committee's note). "In the Ninth Circuit, [a]n  
2 amendment adding a party plaintiff relates back to the date of the original pleading  
3 only when: 1) the original complaint gave the defendant adequate notice of the  
4 claims of the newly proposed plaintiff; 2) the relation back does not unfairly  
5 prejudice the defendant; and 3) there is an identity of interests between the original  
6 and newly proposed plaintiff." Id. (citing Rosenbaum v. Syntex Corp., 95 F.3d  
7 922, 935 (9th Cir. 1996)).

8 The previous complaints filed in this action did not give Defendants  
9 "adequate notice of the claims" of the Convertible Note purchasers. Instead, the  
10 prior complaints focused solely on the claims of those who purchased DDi  
11 common stock. See, e.g., CAC ¶ 1 ("[Plaintiffs] bring this action on their own  
12 behalf and on behalf of all persons or entities who purchased DDi Corp. common  
13 stock between December 19, 2000 and April 29, 2002 including all persons who  
14 acquired DDi common stock pursuant to, or traceable to, its February 14, 2001  
15 offering."). Cf. Rembold v. Pacific First Fed. Sav. Bank, 1989 U.S. Dist. LEXIS  
16 3953, at \*4 (D. Or. Apr. 7, 1989) ("The fact that the . . . plaintiffs instituted  
17 litigation concerning the stock transaction of [the defendant] does not put the  
18 defendants on notice as to every other person who purchased the stock."). This  
19 has remained true throughout this litigation despite the fact that Plaintiffs must  
20 have known that the Convertible Notes were issued along with the common stock  
21 in the Offering. See Prospectus at Title Page ("Concurrently with this offering, we  
22 are offering \$100,000,000 aggregate principal amount of 5 1/4% convertible  
23 subordinated notes due 2008.").

24 Furthermore, there is a lack of an "identity of interest" between the "original  
25 plaintiffs" – i.e., those who purchased DDi common stock pursuant to or traceable  
26 to the Prospectus – and the "newly proposed plaintiffs" – i.e., those who purchased  
27 Convertible Notes. In fact, these two groups purchased entirely different  
28 securities. Cf. Rosenbaum, 95 F.3d at 935 (no identity-of-interest in securities

1 fraud class action where “newly proposed class members bought stock at different  
2 values and after different disclosures and statements”). For both of these reasons,  
3 the Convertible Note purchasers’ claims do not “relate back” to the previous  
4 complaints’ filing dates. Accordingly, the statute of limitations bars Plaintiffs’  
5 Securities Act claims insofar as they are asserted on behalf of those who  
6 purchased the Convertible Notes.<sup>9</sup>

### 7 **B. Applicable Pleading Standard**

8 In ruling on the CAC, the court found that all of Plaintiffs’ claims, including  
9 their Securities Act claims, were “grounded in fraud,” and were therefore subject  
10 to Rule 9(b)’s heightened pleading requirements for “averments of fraud.” See In  
11 re DDi, 2005 U.S. Dist. LEXIS 1056, at \*57-62. Analyzing Plaintiffs’ allegations  
12 under Rule 9(b)’s heightened pleading standard, the court concluded that Plaintiffs  
13 had failed to particularly allege that any statement in the Prospectus was materially  
14 false and misleading. See id. at 62-75.

15 In the SAC, Plaintiffs have omitted all references to fraud and no longer  
16 assert fraud-based Exchange Act claims. Furthermore, they now contend that

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17  
18 <sup>9</sup> Almost all of the cases cited by Plaintiffs in support of their “relation back”  
19 argument are inapplicable to the present case due to the fact that they discuss whether  
20 new claims, not new claims by new plaintiffs, “relate back.” See Martell v. Trilogy Ltd.,  
21 872 F.2d 322 (9th Cir. 1989); E.W. French & Sons, Inc. v. Gen. Portland Inc., 885 F.2d  
22 1392, 1395-96 (9th Cir. 1989); Percy v. San Francisco Gen. Hosp., 841 F.2d 975, 978  
23 (9th Cir. 1988); Grattan v. Burnett, 710 F.2d 160, 163 (4th Cir. 1983); Santana v. Holiday  
24 Inns, Inc., 686 F.2d 736, 738-40 (9th Cir. 1982); In re Digital Microwave Corp. Sec.  
25 Litig., 1992 U.S. Dist. LEXIS 18469, at \*5-6 (N.D. Cal. Oct. 19, 1992). Plaintiffs also  
26 inappropriately cite an unpublished Ninth Circuit decision. See Viall v. Scott, 1991 U.S.  
27 App. LEXIS 22051 (9th Cir. 1991) (“This disposition is not appropriate for publication  
28 and may not be cited to or by the courts of this circuit except as provided by the 9th Cir.  
R. 36-3.”). Finally, Plaintiffs cite In re Network Assoc., Inc. II Sec. Litig., 2003 U.S.  
Dist. LEXIS 14442, at \*24-25 (N.D. Cal. Mar. 25, 2003), which is inapplicable to the  
present case due to the fact that the plaintiffs in that case added claims on behalf of new  
plaintiffs who had purchased the same security as the original plaintiffs, rather than – as is  
the case here – on behalf of new plaintiffs who purchased an entirely different security.

1 Defendants' alleged wrongful conduct was the result of negligence, not fraud.  
2 Consequently, they argue that the SAC is not "grounded in fraud," is not subject to  
3 Rule 9(b), and is instead subject only to Rule 8(a)'s notice pleading model.  
4 Defendants disagree, arguing that Rule 9(b) continues to apply because:  
5 (1) Plaintiffs are bound to the fraud-based allegations in the CAC, and (2) the SAC  
6 independently "sounds in fraud." Because the SAC contains no more detail than  
7 the CAC, Defendants conclude that the SAC must be dismissed for failure to  
8 satisfy Rule 9(b).

9 1. Effect of Fraud-Based Allegations in the CAC

10 Defendants' first argument is that Rule 9(b) continues to apply to Plaintiffs'  
11 claims because Plaintiffs are bound by the fraud-based allegations in the CAC. In  
12 particular, Defendants argue that Plaintiffs cannot now claim that conduct once  
13 alleged to be "fraudulent" was actually "negligent." According to Defendants,  
14 these allegations are contradictory, and Plaintiffs are bound to their former fraud-  
15 based claims, which are subject to – and fail to meet – Rule 9(b)'s heightened  
16 pleading standard.

17 This argument fails. Although a plaintiff generally cannot amend a  
18 complaint to assert facts contradicting those alleged in an earlier complaint, see,  
19 e.g., Reddy v. Litton Indus., Inc., 912 F.2d 291, 296-97 (9th Cir. 1990),  
20 Defendants cite no authority for the proposition that a plaintiff cannot amend a  
21 complaint to assert that conduct once alleged to be intentional or fraudulent was  
22 actually negligent. Indeed, the conduct at issue here – the inclusion of false and  
23 misleading statements in a prospectus – could just as easily result from negligence  
24 as from fraud. Therefore, Plaintiffs were entitled to change the theory of their case  
25 to one of negligence, and the SAC has now superseded the CAC and is the  
26 operative complaint. See Hal Roach Studios, Inc. v. Richard Feiner & Co., Inc.,  
27 896 F.2d 1542, 1546 (9th Cir. 1990) ("an amended pleading supersedes the  
28 original"). See also Kelley v. Crosfield Catalysts, 135 F.3d 1202, 1204 (7th Cir.

1 1998) (“It is well-established that an amended pleading supersedes the original  
2 pleading; facts not incorporated into the amended pleading are considered *functus*  
3 *officio*.”); Loux v. Rhay, 375 F.2d 55, 57 (9th Cir. 1967) (same); Lubin v. Chicago  
4 Title & Trust Co., 260 F.2d 411, 413 (7th Cir. 1958) (same); 3 James Wm. Moore  
5 et al., Moore’s Federal Practice ¶ 15.17[3] (3d ed. 1997) (same). Consequently,  
6 Defendants’ arguments regarding the proper pleading standard must be based on  
7 the allegations in the SAC, not those found in the CAC. See Bullen v. Bretteville,  
8 239 F.2d 824, 833 (9th Cir. 1956) (“Once amended, the [former complaint] no  
9 longer performs any function as a pleading and cannot be utilized to aid a  
10 defective amendment.”) (citations omitted). Accordingly, the court rejects  
11 Defendants’ argument that Rule 9(b) applies to the SAC because of the CAC’s  
12 allegations.

## 13 2. Allegations in the SAC

14 Defendants’ second argument is that Plaintiffs’ Securities Act claims as  
15 alleged in the SAC independently “sound in fraud” and are therefore subject to  
16 Rule 9(b). This argument also fails.

17 In In re Daou Sys., Inc., Sec. Litig. (“In re Daou”), 397 F.3d 704 (9th Cir.  
18 2005), the Ninth Circuit recently clarified when Securities Act claims (or certain  
19 portions thereof) are subject to Rule 9(b)’s heightened pleading requirements:

20 Although [the applicable portions of the Securities Act] do[] not  
21 contain an element of fraud, a plaintiff may nonetheless be subject to  
22 Rule 9(b)’s particularity mandate if his complaint “sounds in fraud”:  
23 “[T]he plaintiff may allege a unified course of fraudulent conduct and  
24 rely entirely on that course of conduct as the basis of a claim. In that  
25 event, the claim is said to be ‘grounded in fraud’ or to ‘sound in  
26 fraud,’ and the pleading of that claim as a whole must satisfy the  
27 particularity requirement of Rule 9(b).” Vess v. Ciba-Geigy Corp.  
28 USA, 317 F.3d 1097, 1103-04 (9th Cir. 2003).

1 In a case where fraud is not an essential element of a claim, only  
2 allegations of fraudulent conduct must satisfy the heightened pleading  
3 requirements of Rule 9(b). Allegations of non-fraudulent conduct  
4 need satisfy only the ordinary notice pleading standards of Rule 8(a).  
5 As the Fifth Circuit [has written]: "Where averments of fraud are  
6 made in a claim in which fraud is not an element, an inadequate  
7 averment of fraud does not mean that no claim has been stated. The  
8 proper route is to disregard averments of fraud not meeting Rule  
9 9(b)'s standard and then ask whether a claim has been stated." . . .  
10 [T]he Eighth Circuit [has] elaborated: "The only consequence of a  
11 holding that Rule 9(b) is violated with respect to a [Securities Act]  
12 claim would be that any allegations of fraud would be stripped from  
13 the claim. The allegations of innocent or negligent misrepresentation,  
14 which are at the heart of a [Securities Act] claim, would survive."  
15 Thus, if particular averments of fraud are insufficiently pled under  
16 Rule 9(b), a district court should "disregard" those averments or  
17 "strip" them from the claim. The court should then examine the  
18 allegations that remain to determine whether they state a claim.

19 A district court need not rewrite a deficient complaint however. Rule  
20 9(b) may prove fatal to . . . Securities Act claims "grounded in fraud"  
21 when the complaint makes a "wholesale adoption" of the securities  
22 fraud allegations for purposes of the Securities Act claims. In such  
23 cases, a district court is not required to sift through allegations of  
24 fraud in search of some "lesser included" claim of strict liability. It  
25 may dismiss. If it does so, it should ordinarily accept a proffered  
26 amendment that either pleads with the requisite particularity or drops  
27 the defective allegations and still states a claim.

28 In re Daou, 397 F.3d at 723 (selected citations and quotation marks omitted).

The SAC does not allege "a unified course of fraudulent conduct"  
implicating Rule 9(b). Instead, it is rooted in allegations of negligence. See, e.g.,  
SAC ¶¶ 41, 44(c), 95-96, 106, 113. Such allegations clearly do not "sound in  
fraud." See Rombach v. Chang, 355 F.3d 164, 170 (2d Cir. 2004) ("[S]everal  
circuits have distinguished between allegations of fraud and allegations of

1 negligence, applying Rule 9(b) only to claims pleaded under Section 11 and  
2 Section 12(a)(2) that sound in fraud.”); In re Dynegy, Inc. Sec. Litig., 339 F. Supp.  
3 2d 804, 827 (S.D. Tex. 2004) (“When § 11 claims are grounded in negligence and  
4 not in fraud there is no scienter requirement, and the plaintiff need only satisfy the  
5 liberal pleading requirements of Rule 8(a).”). Compare Rombach, 355 F.3d at 178  
6 (“[Plaintiffs’] claims are not subject to the heightened pleading requirements of  
7 Rule 9(b), because they sound in negligence: ‘each of the Underwriter Defendants  
8 owed to the purchasers of the shares of [the company] . . . the duty to make a  
9 reasonable and diligent investigation of the statements contained in the  
10 Prospectus”), Schwartz v. Celestial Seasonings, Inc., 124 F.3d 1246, 1252 (10th  
11 Cir. 1997) (“the [Securities Act] claim . . . is not premised on fraud . . . [because]  
12 the Complaint[] alleges that defendants failed to make a ‘reasonable investigation’  
13 of the statements contained in the Registration Statements and Prospectuses”)  
14 (emphasis omitted), and In re Calpine Corp. Sec. Litig., 288 F. Supp. 2d 1054,  
15 1078 (N.D. Cal. 2003) (following allegation sounds in negligence: ‘None of the  
16 defendants . . . made a reasonable investigation or possessed reasonable grounds  
17 for the belief that the challenged statements . . . were accurate and complete in all  
18 material respects.’), with SAC ¶ 41 (“Each of the defendants owed to the  
19 purchasers of DDi stock and the Convertible Notes . . . the duty to make a  
20 reasonable and diligent investigation of the statements contained in the . . .  
21 Prospectus . . .”). Consequently, Rule 9(b) does not apply to the entire SAC.<sup>10</sup>

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23 <sup>10</sup> Defendants attempt to avoid this result by citing a series of cases holding that a  
24 complaint may still be “grounded in fraud,” and therefore subject to Rule 9(b), despite the  
25 fact that it disclaims reliance on fraud. The court concurs with the proposition, but finds  
26 the facts of these cases inapposite. See, e.g., Castlerock Management, LTD v. Ultralife  
27 Batteries, Inc., 68 F. Supp. 2d 480, 486 (D.N.J. 1999) (complaint alleging that defendants  
28 “participated in the alleged wrongdoing, in part, in order to continue and prolong the  
illusion of [the company’s] financial growth, to inflate [the company’s] publicly reported  
(continued . . .)



Furthermore, the SAC does not contain any particular “averments of fraud” triggering Rule 9(b). Instead, each and every allegation in the SAC is rooted in the assertion that the Prospectus was false and misleading as a result of Defendants’ negligence.<sup>11</sup> Consequently, Rule 9(b) does not apply to any of the SAC’s allegations. Accordingly, Plaintiffs’ Securities Act claims are subject to Rule 8(a)’s notice pleading model, not Rule 9(b). All of Defendants’ arguments premised upon Rule 9(b) are therefore rejected.

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revenues and earnings, to conceal the adverse facts concerning [the company’s] operations, financial condition and business and to permit [the company] to raise millions of dollars pursuant to the Offering”); In re Anchor Gaming Sec. Litig., 33 F. Supp. 2d 889, 892-93 (D. Ariz. 1999) (complaint alleging that “certain . . . [d]efendants decided to take advantage of the rising price of . . . common stock,” that while “the price of stock dropped significantly following [an] announcement, defendants acted quickly to stem this decline,” that a particular announcement “had the desired effect” of driving up the price of the company’s stock, and that defendants decided to sell a substantial portion of their equity in the company while certain facts were “still concealed”); In re GameTech Int’l, Inc. Sec. Litig., 1999 U.S. Dist. LEXIS 22289, at \*13 (D. Ariz. June 1, 1999) (relying, in part, on allegation that defendants “failed to [meet their duty to refrain from misleading investors] by concealing then-existing adverse facts affecting [the company’s] business and prospects”); In re Computervision Corp. Sec. Litig., 869 F. Supp. 56, 63-64 (D. Mass. 1994) (complaint alleging, among other things, that “in order to give the offerings a coloration of legitimacy and arm’s-length pricing and to prop up the immediate aftermarket prices, Shearson manipulated the market for Computervision securities with secret promises and inducements to customers to participate in the Offerings”).

<sup>11</sup> Defendants repeatedly argue that the SAC contains “averments of fraud” because it alleges: (1) that Defendants knowingly failed to disclose that DDi had been sluggish beginning in the fourth quarter of 2000; and (2) that Defendants had engaged in “accounting improprieties” to “mask” – *i.e.*, deliberately conceal – DDi’s deteriorating financial condition. First, the SAC nowhere alleges that Defendants “knowingly” failed to disclose DDi’s financial condition. Second, the SAC alleges that certain accounting improprieties “masked” – *i.e.*, hid from public view – DDi’s financial condition, not that Defendants committed the accounting improprieties or that they did so intentionally to conceal DDi’s financial condition. See SAC ¶¶ 86, 89.

**C. Section 11 Claim**

Plaintiffs assert a claim under § 11(a) of the Securities Act against the Underwriter Defendants and those defendants who signed the Prospectus (*i.e.*, Dimick, McMaster, Gisch, Benham, Dominik, Pagliuca, Zide, and Conrad). Plaintiffs' claim is rooted in the allegation that the Prospectus was materially false and misleading for the six reasons outlined above. See supra Part II.<sup>12</sup>

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<sup>12</sup> As mentioned, Plaintiffs allege that the Prospectus was materially false and misleading on the following grounds:

[1] DDi's purportedly exceptional full year and fourth quarter 2000 financial results [included in the Prospectus] were materially false and misleading as they included revenue to which DDi was not entitled under GAAP or DDi's internal accounting policy.

[2] [T]he February Prospectus misrepresented the amount of DDi customers and failed to disclose that DDi had lost many of its historically largest customers. Specifically, even if DDi included its smallest customers (under \$10K per year), its total customer base was approximately 500, not 2000. As for specific clients, by the fourth quarter 2000, DDi was booking very little or no business from, *inter alia*, Alcatel, Redback, Intel, Marconi, 3Com, IBM, Nortel, and Cisco.

[3] [T]he February Prospectus misrepresented and omitted to disclose that by no later than the fourth quarter of 2000, DDi's quick-turn and value-added businesses had suffered precipitous declines and DDi's transaction pipeline had dried up.

[4] [T]he February Prospectus misrepresented and omitted to disclose that in 2000, DDi's revenues were as dependent on the high-premiums DDi reaped from its value-added services business as those from its quick-turn business, and that by late-2000 DDi was not receiving high-premiums on its value-added services.

[5] [T]he statements concerning DDi's intent to increase and maximize its manufacturing capacity [were] misleading and incomplete as DDi

(continued . . .)

1 Section 11 establishes liability for false and misleading statements made in  
2 a registration statement. See 15 U.S.C. § 77k. It provides as follows:

3 In case any part of the registration statement . . . contained an untrue  
4 statement of material fact or omitted to state a material fact required  
5 to be stated therein or necessary to make the statements therein not  
6 misleading, any person acquiring such security . . . may . . . sue –

7 (1) every person who signed the registration statement;

8  
9 (2) every person who was a director of (or person performing similar  
10 functions) or partner in the issuer at the time of the filing of the part  
11 of the registration statement with respect to which his liability is  
asserted;

12 (3) every person who, with his consent, is named in the registration  
13 statement as being or about to become a director, person performing  
14 similar functions, or partner; . . . [and]

15 (5) every underwriter with respect to such security.  
16

17 Id. To assert a claim under § 11, the plaintiff must allege: “(1) that the registration  
18 statement contained an omission or misrepresentation, and (2) that the omission or  
19 misrepresentation was material, that is, it would have misled a reasonable investor  
20 about the nature of his or her investment.” In re Daou, 397 F.3d at 722-23. “No  
21

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22 experienced significant layoffs and actually reduced operations in early  
23 2001.

24 [6] DDi’s glowing outlook was untenable and incomplete as DDi had  
25 suffered a precipitous loss of both value-added and quick-turn business  
26 leading up to the February Offering such that DDi’s sales pipeline was  
27 depleted entering 2001.

28 SAC ¶¶ 73-79.

1 scienter is required for liability under § 11; defendants will be liable for innocent  
2 or negligent material misstatements or omissions.” Id. at 723.

3 An omission is considered “material” if there is “a substantial likelihood  
4 that, under all the circumstances, the omitted fact would have assumed actual  
5 significance in the deliberations of a reasonable shareholder.” In re McKesson  
6 HBOC, Inc. Sec. Litig., 126 F. Supp. 2d 1248, 1259 (N.D. Cal. 2000). “Put  
7 another way, there must be a substantial likelihood that the disclosure of the  
8 omitted fact . . . would have been viewed by the reasonable investor as having  
9 significantly altered the ‘total mix’ of information made available.” Id. (citing  
10 TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976)). See also In re Stac  
11 Elec. Sec. Litig. (“In re Stac”), 89 F.3d 1399, 1408 (9th Cir. 1996) (same). A  
12 misrepresentation is material when an investor would attach importance to it in  
13 making an investment decision. See Basic, Inc. v. Levinson, 485 U.S. 224, 231  
14 (1988). “Although a court may dismiss a claim on the ground that a misstatement  
15 or omission was not material, the standard for doing so is high.” In re Sterling  
16 Foster & Co., Inc., Sec. Litig., 222 F. Supp. 2d 216, 262 (E.D.N.Y. 2002)  
17 (quotation marks omitted). In fact, “a complaint may not properly be dismissed  
18 pursuant to Rule 12(b)(6) . . . on the ground that the alleged misstatements or  
19 omissions are not material unless they are so obviously unimportant to a  
20 reasonable investor that reasonable minds could not differ on the question of their  
21 importance.” Id. at 262-63 (quoting Goldman v. Belden, 754 F.2d 1059, 1067 (2d  
22 Cir. 1985)). “Moreover, a court deciding a motion to dismiss shall be mindful that  
23 the issue of whether a statement or omission is material is usually a question for  
24 the fact finder.” Id. (citing TSC Indus., Inc., 426 U.S. at 450). See also In re  
25 Stac, 89 F.3d at 1405 (“The ‘materiality’ of an omission is a fact-specific  
26 determination that should ordinarily be assessed by a jury. [O]nly if the adequacy  
27 of the disclosure or the materiality of the statement is so obvious that reasonable  
28 minds could not differ are these issues appropriately resolved as a matter of law.”)

(citations and quotation marks omitted). See generally In re Network Assoc., Inc. II Sec. Litig., 2003 U.S. Dist. LEXIS 14442, at \*15 (N.D. Cal. Mar. 25, 2003) (“[W]hether a statement or omission is misleading to potential investors requires delicate assessments of the inferences a ‘reasonable shareholder’ would draw from a given set of facts and the significance of those inferences to him, and these assessments are peculiarly one for the trier of fact.”) (citations and quotation marks omitted).

Defendants argue that Plaintiffs’ § 11 claim must be dismissed because: (1) the Prospectus did not include any material false and misleading statements or omissions, (2) the “negative causation” defense bars Plaintiffs’ Securities Act claims, and (3) the allegedly false and misleading statements in the Prospectus are not actionable due to the puffery doctrine, the bespeaks caution doctrine, and/or the PSLRA’s safe harbor provision.<sup>13</sup>

1. Material False and Misleading Statements and/or Omissions in the Prospectus

Despite Defendants’ arguments to the contrary, Plaintiffs have adequately alleged that the Prospectus was materially false and misleading with respect to at least three matters. First, Plaintiffs adequately allege that the financial reports included in the Prospectus were materially false and misleading. According to Plaintiffs, these financial reports were overstated due to “accounting improprieties,” including DDi’s tendency to “recognize[] revenue on (1) the premature shipment of orders to clients (e.g., Watkins Johnson, Marconi) prior to the authorized delivery date; and (2) the shipment of orders from one DDi facility

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<sup>13</sup> Defendants also argue that Plaintiffs do not have standing to assert the § 11 claim. While lead plaintiffs Poppe and Schneider may lack standing, see Joint Decl. of Poppe, Schneider, Skolmick, and Rust ¶ 4 (stating earlier in these proceedings that they do not have standing to assert § 11 claim), there is no dispute that representative plaintiff Watson has standing.

1 to another.” SAC ¶ 80. Plaintiffs allege that these practices violated GAAP and  
2 DDi’s own internal accounting policies. Id. ¶ 79.

3 Defendants contend that Plaintiffs’ allegations regarding these accounting  
4 improprieties are insufficient because: (1) they fail to meet the particularity  
5 requirement of Rule 9(b), and (2) they fail to demonstrate that the Prospectus was  
6 “materially” false and misleading. Defendants’ first argument fails because  
7 Plaintiffs’ allegations are subject to Rule 8(a), not Rule 9(b). Defendants’ second  
8 argument fails due to the fact that Plaintiffs expressly allege that these accounting  
9 improprieties caused the Prospectus to be “materially” false and misleading, and  
10 because Plaintiffs allege that, as an example, these accounting improprieties were  
11 responsible for approximately 25% of one of DDi’s facility’s quarterly revenues.  
12 See id. ¶¶ 80, 89. Given Rule 8(a)’s extremely liberal pleading standard, see In re  
13 Initial Public Offering Sec. Litig., 241 F. Supp. 2d 281, 322-24 (S.D.N.Y. 2003),  
14 and the fact that a complaint may not be dismissed on materiality grounds unless  
15 the misstatements or omissions “are so obviously unimportant to a reasonable  
16 investor that reasonable minds could not differ on the question of their  
17 importance,” see In re Sterling Foster & Co., Inc., Sec. Litig., 222 F. Supp. 2d at  
18 262, the court finds that Plaintiffs have sufficiently alleged that the Prospectus was  
19 materially false and misleading as a result of these alleged “accounting  
20 improprieties.”

21 Second, Plaintiffs have adequately alleged that the Prospectus  
22 “misrepresented the amount of DDi customers . . . .” SAC ¶ 74. See also id. ¶ 68.  
23 While the Prospectus stated that DDi had “over 2000 customers,” Plaintiffs allege  
24 that DDi actually had only 500 customers. Id. ¶¶ 68, 74. Defendants argue that  
25 Plaintiffs’ allegations regarding this matter fail to satisfy Rule 9(b). However, as  
26 mentioned, Rule 9(b) is inapplicable. Defendants also advance certain arguments  
27 based upon the allegations found in the CAC. However, as also mentioned, the  
28 SAC has superseded the CAC. See Bullen, 239 F.2d at 833. Finally, Defendants



1 argue that this alleged misstatement regarding the number of DDi customers was  
2 immaterial. However, it is not “obvious” that a “reasonable investor” would find  
3 it immaterial that a company touting its “large and diverse customer base”  
4 misrepresented the number of its customers by 300%. See SAC ¶ 67 (quoting  
5 Prospectus as stating: “We believe that our large and diverse customer base also  
6 makes us less vulnerable to individual customer shifts in demand.”). Therefore,  
7 Plaintiffs have sufficiently alleged that the Prospectus made a material  
8 misrepresentation with respect to the number of DDi customers.<sup>14</sup>

9 Third, Plaintiffs have adequately alleged that the Prospectus misrepresented  
10 the recent and then-current state of DDi’s business affairs. See id. ¶ 75. While the  
11 Prospectus represented that DDi had experienced “strong demand” in the fourth  
12 quarter of 2000 and included various other statements indicating that DDi had  
13 been and was doing well, Plaintiffs allege that in reality, DDi’s business was  
14 hemorrhaging in the fourth quarter of 2000. Id. ¶¶ 64, 65, 75. For example,  
15 Plaintiffs allege that by the fourth quarter of 2000, “the overall demand for quick-  
16 turn and value-added PCBs [had] dropped off precipitously,” “[m]any of the  
17 customers . . . [had] tried to cancel [orders],” “many of DDi’s customers [had]  
18 stopped doing business with [DDi],” “DDi’s sales pipeline [had] dried up,” and  
19 “DDi was forced to implement across the board employee pay cuts.” See id. ¶¶ 56,  
20 64, 65, 69, 77. Defendants argue that these allegations fail to satisfy Rule 9(b),  
21 and fail to demonstrate that the Prospectus was “materially” false and misleading.  
22 However, Rule 9(b) is inapplicable, and it is not “obvious” that a “reasonable  
23  
24  
25

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26  
27 <sup>14</sup> Defendants also quibble over the definition of “customer” and “customer base.”  
28 These types of arguments are more appropriate for summary judgment or trial than a Rule  
12(b)(6) motion to dismiss.

investor” would have found this information immaterial.<sup>15</sup> Consequently, Plaintiffs have adequately alleged that the Prospectus was materially false and misleading with respect to this matter.

Thus, Plaintiffs have sufficiently alleged that the Prospectus was materially false and misleading with respect to at least three matters. The court need not consider whether Plaintiffs have adequately alleged that the Prospectus was materially false and misleading with respect to other matters. See Cooper v. Pickett, 137 F.3d 616, 623 (9th Cir. 1997) (“Since we conclude that, if proved, many of the allegations of the complaint state causes of action, we need not at this juncture in the case opine on some of the closer questions, such as whether the rosy forecasts were known to be false and are therefore actionable. These judgments should be made after discovery is complete.”); In re Stratosphere Corp. Sec. Litig., 1 F. Supp. 2d 1096, 1118 (D. Nev. 1998) (same). See also Sutton v. Bernard, 2001 U.S. Dist. LEXIS 11610, at \*14 (N.D. Ill. Aug. 6, 2001) (“Nonetheless, we need not parse through each and every alleged misstatement contained in the complaint to determine if it is actionable. It is sufficient for pleading purposes that at least some of the GAAP violations (and other material misstatements and omissions) alleged by plaintiffs are actionable.”); In re Oxford Health Plans, Inc., 187 F.R.D. 133, 141 (S.D.N.Y. 1999) (if court has concluded that some of the statements in document are actionable, “it is unwise” at the pleading stage for “the Court to parse out potentially no statements and at most only very few statements [as not actionable] while other statements remain[] in the case to be tried.”). Accordingly, the court rejects Defendants’ argument that

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<sup>15</sup> Defendants also argue that Plaintiffs’ allegation that DDi’s business was hemorrhaging in the fourth quarter of 2000 is untenable in light of the record financial results that DDi experienced in that quarter. However, this argument ignores the fact that Plaintiffs have adequately alleged that DDi’s “record financial results” were inaccurate due to the alleged “accounting improprieties.”

1 Plaintiffs have failed to allege any false and misleading statements (or omissions)  
2 in the Prospectus.

3 2. Negative Causation Defense

4 Defendants also argue that Plaintiffs' Securities Act claims are barred by the  
5 negative causation defense.

6 Section 11(e) of the Securities Act provides the measure of damages for  
7 Securities Act claims:

8 The suit . . . may be to recover such damages as shall represent the  
9 difference between the amount paid for the security (not exceeding  
10 the price at which the security was offered to the public) and (1) the  
11 value thereof as of the time such suit was brought, or (2) the price at  
12 which such security shall have been disposed of in the market before  
13 suit, or (3) the price at which such security shall have been disposed  
14 of after suit but before judgment if such damages shall be less than  
15 the damages representing the difference between the amount paid for  
16 the security (not exceeding the price at which the security was offered  
brought . . . .

17 15 U.S.C. § 77k(e).

18 Because § 11(a) imposes strict liability for misrepresentations contained in a  
19 registration statement, any decline in value is presumed to be caused by the  
20 alleged misrepresentation. See Akerman v. Oryx Communications, Inc., 810 F.2d  
21 336, 340 (2d Cir. 1987). See also Casella v. Webb, 883 F.2d 805, 808 (9th Cir.  
22 1989) ("the buyer need not show any causal connection between the  
23 misrepresentation and his damage"). Section 11(e), however, provides the  
24 following affirmative defense:

25 [I]f the defendant proves that any portion or all of such damages  
26 represents other than the depreciation in value of such security  
27 resulting from such part of the registration statement, with respect to  
28 which his liability is asserted, not being true or omitting to state a

1 material fact required to be stated therein or necessary to make the  
2 statements therein not misleading, such portion of or all such  
3 damages shall not be recoverable.

4 15 U.S.C. § 77k(e).

5 “This defense is known as the ‘negative causation defense.’” In re Dynegy,  
6 Inc. Sec. Litig., 339 F. Supp. 2d at 867 (citing Akerman, 810 F.2d at 340).

7 “Where a defendant proves that the decline in the value of a security was not  
8 caused by the material omissions or misstatements in the registration statement,  
9 plaintiff is not entitled to recover any damages.” Id. (citing Akerman, 810 F.2d at  
10 340). “The defendant bears the burden of proof on this defense,” and the burden is  
11 a “heavy” one. Id. at 867-68 (citing Akerman, 810 F.2d at 340). “Loss causation”  
12 can be used as a ground for dismissal on a Rule 12(b)(6) motion to dismiss only if  
13 the merits of the defense are “apparent on the face of [the] complaint.” See In re  
14 Alamosa Holdings, Inc., 2005 WL 712001, at \*30 (N.D. Tex. Mar. 28, 2005). See  
15 also Cats v. Protection One, Inc., 2001 U.S. Dist. LEXIS 25725, at \*34 (C.D. Cal.  
16 June 4, 2001) (Tevrizian, J.) (same).

17 Defendants argue that the SAC affirmatively asserts that the alleged  
18 misrepresentations and omissions in the Prospectus were not revealed until *after*  
19 the value of DDi common stock plummeted from \$22.00 per share to \$.06 per  
20 share. Consequently, Defendants argue that the SAC demonstrates that the drop in  
21 value of DDi common stock was caused by something other than the alleged  
22 misrepresentations and omissions in the Prospectus. Therefore, Defendants  
23 contend, Plaintiffs’ claims are barred by the negative causation defense.

24 Defendants’ argument fails. The SAC does not affirmatively assert that the  
25 alleged misrepresentations and omissions in the Prospectus were revealed only  
26 after the value of DDi common stock plummeted. For example, it is unclear when  
27 the “accounting improprieties” were revealed or when it was disclosed that DDi  
28 had only 500 customers. Additionally, although the SAC alleges that “[i]nvestors

1 had no reason to believe that DDi's business began to deteriorate in late-2000 until  
2 the Company filed for Bankruptcy [in 2003]," SAC ¶ 90, it also states that "[o]nce  
3 DDi's financial condition became apparent, the Company's stock price fell below  
4 \$1.00 per share, thereby leading to DDi's . . . bankruptcy." *Id.* ¶ 12. The SAC is  
5 at least ambiguous as to whether the alleged misrepresentations and omissions  
6 regarding DDi's financial condition were revealed before or after the drop in value  
7 of DDi common stock. Thus, it is not "apparent on the face" of the SAC that the  
8 loss in value of DDi common stock was caused by something other than the  
9 alleged misrepresentations and omissions in the Prospectus. Accordingly, the  
10 court rejects Defendants' motions insofar as they rely on the negative causation  
11 defense.

### 12 3. Puffery, Bespeaks Caution, and the Safe Harbor Provision

13 Defendants argue that Plaintiffs' Securities Act claims must be dismissed  
14 because the alleged false and misleading statements in the Prospectus are  
15 protected by the puffery doctrine, the bespeaks caution doctrine, and/or the  
16 PSLRA's safe-harbor provision.

#### 17 a. *Puffery*

18 Under the doctrine of "puffery," a corporate insider's vague expressions of  
19 optimism or belief generally cannot serve as the basis for a securities law claim.  
20 See Raab v. General Physics Corp., 4 F.3d 286, 290 (4th Cir. 1993); In re Verifone  
21 Sec. Litig., 784 F. Supp. 1471, 1481 (N.D. Cal. 1992). This doctrine is not  
22 applicable here, at least at this stage in the proceedings. For example, the three  
23 above-mentioned misrepresentations in the Prospectus related to DDi's historical  
24 financial results, the number of its customers, and its success in the fourth quarter  
25 of 2000. They did not relate to "a corporate insider's vague expression of  
26 optimism or belief." Furthermore, the court need not determine at this stage  
27 whether various other alleged misstatements in the Prospectus are protected by the  
28 puffery doctrine. See Cooper, 137 F.3d at 623 (9th Cir. 1997); In re Stratosphere

1 Corp. Sec. Litig., 1 F. Supp. 2d at 1118. See also Sutton, 2001 U.S. Dist. LEXIS  
2 11610, at \*14 (“Nonetheless, we need not parse through each and every alleged  
3 misstatement contained in the complaint to determine if it is actionable. It is  
4 sufficient for pleading purposes that at least some of the GAAP violations (and  
5 other material misstatements and omissions) alleged by plaintiffs are actionable.”);  
6 In re Oxford Health Plans, Inc., 187 F.R.D. at 141 (if court has concluded that  
7 some of the statements in document are actionable, “it is unwise” at the pleading  
8 stage for “the Court to parse out potentially no statements and at most only very  
9 few statements [as not actionable] while other statements remain[] in the case to be  
10 tried.”).

11 *b. Bespeaks Caution and the Safe Harbor Provision*

12 The “bespeaks caution doctrine” provides protection for optimistic  
13 projections accompanied by cautionary language containing relevant specific facts  
14 or assumptions. In re Worlds of Wonder Sec. Litig. (“WOW”), 35 F.3d 1407,  
15 1413 (9th Cir. 1994). The doctrine arises from the application of two fundamental  
16 concepts in securities fraud cases: materiality and reliance. Id. at 1414. When  
17 appropriate cautionary language accompanies forward-looking statements, the  
18 materiality of the forward-looking statements and the reasonableness of reliance  
19 are affected. Id.

20 The PSLRA’s “safe harbor” provision amended the Securities Act, see 15  
21 U.S.C. § 77z-2, and the Exchange Act, see 15 U.S.C. § 78u-5. Similar to the  
22 judicially-created bespeaks caution doctrine, these sections provide protection to  
23 “forward-looking statements.” See In re Infonet Serv. Corp. Sec. Litig. (“In re  
24 Infonet”), 310 F. Supp. 2d 1080, 1103 (C.D. Cal. 2003). The safe harbor  
25 provision provides that a forward-looking statement cannot be the basis of liability  
26 under the Securities Act or the Securities Exchange Act if: (1) the statement is  
27 identified as forward-looking and is accompanied by sufficient cautionary  
28 statements, 15 U.S.C. § 78u-5(c)(1)(A); or (2) the person who made the



forward-looking statement did so without actual knowledge that the statement was false or misleading, 15 U.S.C. § 78u-5(c)(1)(B).

Neither the bespeaks caution doctrine nor the safe harbor provision bars Plaintiffs' Securities Act claims, at least at this stage in the proceedings. As mentioned, Plaintiffs have adequately alleged that the Prospectus misrepresented DDi's historical financial performance, as well as the number of its customers. Neither of these alleged misrepresentations were "forward looking." Consequently, the bespeaks caution doctrine and the safe harbor provision are inapplicable. See In re WRT Energy, 2005 WL 323729, at \*8 (S.D.N.Y. Feb. 9, 2005) ("[A]pplication of the 'bespeaks caution' doctrine is limited only to forward-looking representations, not misrepresentations of present or historical facts.") (citing P. Stolz Family P'ship L.P. v. Daum, 355 F.3d 92, 96-97 (2d Cir. 2004)); In re Complete Mgmt. Inc. Sec. Litig., 153 F. Supp. 2d 314, 340 (S.D.N.Y. 2001) (safe-harbor provisions "apply to forward-looking statements only, and not to material omissions or misstatements of historical fact").<sup>16</sup>

Thus, Plaintiffs have alleged that the Prospectus was materially false and misleading with respect to at least three matters. Furthermore, Plaintiffs' allegations regarding these matters are not barred by the negative causation defense, the puffery doctrine, the bespeaks caution doctrine, or the safe harbor provision. Accordingly, despite Defendants' arguments to the contrary, Plaintiffs

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<sup>16</sup> The court need not determine at this time whether other alleged misstatements and omissions in the Prospectus are rendered inactionable by the bespeaks caution doctrine and/or the safe harbor provision. See Cooper, 137 F.3d at 623 ("Since we conclude that, if proved, many of the allegations of the complaint state causes of action, we need not at this juncture in the case opine on some of the closer questions, such as whether the rosy forecasts were known to be false and are therefore actionable. These judgments should be made after discovery is complete."); In re Stratosphere Corp. Sec. Litig., 1 F. Supp. 2d at 1118. See also Sutton, 2001 U.S. Dist. LEXIS 11610, at \*14; In re Oxford Health Plans, Inc., 187 F.R.D. at 141.

1 have sufficiently alleged a § 11 claim on behalf of those who purchased DDi  
2 common stock pursuant to or traceable to the Prospectus.

3 **D. Section 12(a)(2) Claim**

4 Plaintiffs assert a claim under § 12(a)(2) of the Securities Act against Bain,  
5 certain Individual Defendants (Gisch, McMaster, Dimick, Halvorson, and Peters),  
6 and the Underwriter Defendants. Section 12(a)(2) makes it unlawful for any  
7 person to use any instrumentality of interstate commerce to offer or sell securities  
8 by means of a prospectus or oral communication that includes “an untrue  
9 statement of a material fact or omits to state a material fact necessary in order to  
10 make the statements, in the light of the circumstances under which they were  
11 made, not misleading.” 15 U.S.C. § 77l(a)(2). Defendants argue: (1) that  
12 Plaintiffs’ entire § 12(a)(2) claim must be dismissed because the SAC fails to  
13 plead that the Prospectus contained a material false and misleading statement,  
14 (2) that the § 12(a)(2) claim must be dismissed insofar as it is asserted on behalf of  
15 those who purchased DDi common stock “traceable to” the Prospectus, (3) that the  
16 § 12(a)(2) claim must be dismissed insofar as it is asserted against Bain and the  
17 Individual Defendants because these parties were not “offerors” or “sellers” under  
18 § 12(a)(2), and (4) that the § 12(a)(2) claim must be dismissed insofar as it is  
19 asserted against the Underwriter Defendants because Plaintiffs have failed to  
20 allege which particular underwriter sold them DDi common stock.

21 **1. Material False and Misleading Statements in Prospectus**

22 As mentioned, Plaintiffs have adequately alleged, under Rule 8(a), that the  
23 Prospectus was materially false and misleading with respect to at least three  
24 matters. First, Plaintiffs have sufficiently alleged that “accounting improprieties”  
25 materially skewed the financial results contained in the Prospectus. See supra Part  
26 IV.C.1. Second, Plaintiffs have adequately alleged that the Prospectus materially  
27 misrepresented the number of DDi customers. See id. Third, Plaintiffs have  
28 sufficiently alleged that the Prospectus materially misrepresented the state of

DDi's business. See id. Accordingly, Defendants' motions are denied insofar as they assert that Plaintiffs have failed to allege any materially false and misleading statements in the Prospectus.

2. Section 12(a)(2) Claim Asserted on Behalf of Those Who Purchased DDi Common Stock "Traceable To" the Prospectus

Defendants argue that Plaintiffs' § 12(a)(2) claim must be dismissed insofar as it is asserted on behalf of those who purchased DDi common stock "traceable to," rather than "pursuant to," the Prospectus. "[P]urchasers in private or secondary market offerings are precluded from bringing actions under Section 12(a)(2)." In re Sterling Foster & Co. Inc., Sec. Litig., 222 F. Supp. 2d at 244. See also In re Ultrafem Inc. Sec. Litig., 91 F. Supp. 2d 678, 693-94 (S.D.N.Y. 2000) (same). Therefore, Plaintiffs' § 12(a)(2) claim is dismissed with prejudice insofar as it is asserted on behalf of those who purchased DDi common stock in private or secondary market offerings.

3. Section 12(a)(2) Claim Asserted Against Bain and the Individual Defendants

Section 12(a)(2) imposes liability on a person who "*offers or sells* a security . . . by means of a prospectus . . . which includes an untrue statement of material fact or omits to state a material fact." 15 U.S.C. § 771(a)(2) (emphasis added). A person "offers or sells" a security within the meaning of § 12(a)(2) if the person either: (1) passes title to the securities to the plaintiff, or (2) solicits the purchase, motivated in part by his own financial interests. See Moore v. Kayport Package Express, Inc., 885 F.2d 531, 536 (9th Cir. 1989). See also In re Infonet, 310 F. Supp. 2d at 1100; Griffin v. Paine Webber, Inc., 2001 U.S. Dist. LEXIS 8937, at \*4 (S.D.N.Y. June 29, 2001). Bain and the Individual Defendants argue that they were not "offerors" or "sellers" under § 12(a)(2).

First, Bain and the Individual Defendants assert that they did not "pass title to the securities to the plaintiff[s]" because the Offering occurred via a firm commitment underwriting. Courts have held that "the issuer and its directors and

1 officers [and selling shareholders] do not pass title to persons who buy in [a] firm  
2 commitment underwriting.” In re Infonet, 310 F. Supp. 2d at 1100. “Instead, title  
3 is passed to buyers by the underwriters.” Id. The Offering here was a firm  
4 commitment underwriting. See Prospectus at 78. Consequently, Bain and the  
5 Individual Defendants did not “pass title to the securities to the plaintiff[s].”

6 Second, Bain and the Individual Defendants argue that they did not  
7 “solicit[] the purchase [of the securities], motivated in part by [their] own financial  
8 interests.” Indeed, the facts alleged in the SAC indicate that Bain and the  
9 Individual Defendants, at most, assisted in preparing and issuing the Prospectus.  
10 See SAC ¶ 103. As explained in In re Stratosphere Corp. Sec. Litig., 1 F. Supp. 2d  
11 1096 (D. Nev. 1998), a defendant’s “simple involvement” in the preparation of a  
12 registration statement is insufficient to establish the sort of relationship between a  
13 buyer and seller required for liability under § 12(a)(2). Id. at 1121. Similarly,  
14 “merely proving that [the defendants] signed the allegedly misleading registration  
15 statement or prospectus for a firm commitment offering is insufficient to prove  
16 that [they] were sellers under section 12.” Id. at 1120. See also In re Infonet, 310  
17 F. Supp. 2d at 1101 (same); In re Musicmaker.com Sec. Litig., 2001 WL  
18 34062431, at \*14 n. 9 (C.D. Cal. June 4, 2001) (Snyder, J.) (same); Thomas Lee  
19 Hazen, Treatise on the Laws of Securities Regulation § 7.2 (4th ed. 2002) (“Even  
20 substantial involvement in the preparation of registration and offering materials  
21 will not create liability unless there is also active involvement in the negotiations  
22 leading to the sale in question.”).<sup>17</sup> Thus, Plaintiffs have failed to allege that Bain

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23  
24 <sup>17</sup> Plaintiffs request that the court ignore this precedent and side with those courts  
25 holding that § 12(a)(2) automatically extends liability to officers and directors who sign  
26 the prospectus and registration. See, e.g., In re National Golf Properties Inc. Sec. Litig.,  
27 2003 U.S. Dist. LEXIS 4321, at \*9 (C.D. Cal. Mar. 18, 2003) (King, J.); In re Proxima  
28 Corp. Sec. Litig., 1994 WL 374306, at \*5 (S.D. Cal. May 3, 1994); Keegan Mgt. Co. Sec. Litig., 1991 WL 253003, at \*8 (N.D. Cal. 1991). The court declines this invitation for the reasons set forth in In re Infonet, 310 F. Supp. 2d at 1100-02.

1 and the Individual Defendants “solicited” the purchase of securities in the  
2 Offering. Accordingly, Plaintiffs have failed to allege that Bain and the Individual  
3 Defendants were “offerors” or “sellers” under § 12(a)(2), and Plaintiffs’ § 12(a)(2)  
4 claim against these defendants is dismissed without prejudice.

5 4. Section 12(a)(2) Claim Against the Underwriter Defendants

6 The Underwriter Defendants argue that Plaintiffs’ § 12(a)(2) claim against  
7 them must be dismissed because Plaintiffs have failed to allege which particular  
8 underwriter sold them DDi common stock in the Offering. Section 12(a)(2)  
9 requires privity between a plaintiff and the seller of the securities at issue – it  
10 permits suit against the seller of a security only by “the person purchasing such  
11 security from him.” 15 U.S.C. § 77l(a)(2); In re IteL Sec. Litig., 89 F.R.D. 104,  
12 116 (N.D. Cal. 1981) (“§ 12 contemplates only an action by a buyer against his  
13 immediate seller”) (citations omitted). “Therefore, this privity requirement means  
14 that if a plaintiff wishes to sue a seller of stock under § 12(a)(2), he must have  
15 bought the stock from that seller; a plaintiff cannot sue a seller from whom he did  
16 not purchase.” Danis v. USN Communications, Inc., 189 F.R.D. 391, 400 (N.D.  
17 Ill. 1999).

18 Representative plaintiff Watson alleges that he “acquired 100 shares of DDi  
19 common stock [from one of the underwriters] in the February Offering pursuant to  
20 the Prospectus.” SAC ¶ 20. He does not allege which underwriter(s) sold him  
21 these 100 shares. Consequently, the Underwriter Defendants argue that Plaintiffs,  
22 apparently represented by Watson with respect to this matter, cannot assert a  
23 § 12(a)(2) claim against any particular underwriter.

24 In In re Westinghouse Sec. Litig. (“In re Westinghouse”), 90 F.3d 696 (3d  
25 Cir. 1996), the Third Circuit rejected this argument. Id. at 717-19. The plaintiffs  
26 in In re Westinghouse alleged that “[e]ach member of the Underwriter Class sold  
27 [company] stock to members of the [plaintiff] class” and that “the underwriter  
28

1 defendants sold [the] securities 'directly to plaintiffs and other Class members.'"

2 Id. at 717. The district court dismissed the plaintiffs' § 12(a)(2) claim, holding:

3 [P]laintiffs must allege, to state a viable Section 12(2) cause of action,  
4 that the underwriter defendants were "sellers" within the meaning of  
5 Section 12(2). That is, there must be an allegation that a particular  
6 proposed defendant sold or solicited the sale of [the company's]  
7 securities to the individual plaintiffs. This element is lacking.

8 Id. at 718 (quoting district court opinion).

9 The Third Circuit reversed, stating that although it "agree[d] with the  
10 district court that plaintiffs must allege that the underwriter defendants were  
11 section 12(2) sellers," there was no support "for the district court's statement that,  
12 in order to achieve this, plaintiffs are required [at the pleading stage] to allege  
13 which underwriter sold securities to each plaintiff." Id. The court stated that  
14 "absent a particularity requirement, plaintiffs must provide a short and plain  
15 statement showing that the underwriter defendants are statutory sellers and that  
16 plaintiffs purchased securities from them." Id. The court found that the plaintiffs'  
17 allegations satisfied this lenient standard:

18 We find that plaintiffs satisfied this requirement and stated a section  
19 12(2) claim against the underwriter defendants. Taken in the light  
20 most favorable to plaintiffs, the first amended complaint alleges that  
21 each of the underwriter defendants sold [the company's] securities  
22 directly to plaintiffs and that each plaintiff purchased [the company's]  
23 securities directly from an underwriter defendant.

24 Id.

25 The court finds In re Westinghouse persuasive. Furthermore, Plaintiffs'  
26 allegations are similar to those proffered by the plaintiffs in In re Westinghouse.  
27 For example, Plaintiffs allege that each of the Underwriter Defendants sold DDi  
28 common stock directly to certain plaintiffs in the Offering, see SAC ¶¶ 36-39, and



1 that these plaintiffs, including Watson, purchased the common stock directly from  
2 an underwriter defendant. See id. ¶¶ 20, 42-43. Furthermore, as noted in In re  
3 Westinghouse, Plaintiffs need not allege “which underwriter sold securities to  
4 each plaintiff.” Thus, Plaintiffs have adequately alleged that the Underwriter  
5 Defendants were statutory sellers under § 12(a)(2). Accordingly, the court rejects  
6 Defendants’ argument that Plaintiffs’ § 12(a)(2) claim against the Underwriter  
7 Defendants must be dismissed because Plaintiffs have failed to plead which  
8 particular underwriter sold them DDi common stock.<sup>18</sup>

9 **E. Section 15 Claim**

10 Plaintiffs assert a claim under § 15(a) of the Securities Act against Gisch,  
11 McMaster, Dimick, Halvorson, Peters, and Bain. Section 15(a) imposes joint and  
12 several liability upon every person who controls any person liable under sections  
13 11 or 12. 15 U.S.C. § 77o. Section 15(a) provides:

14 Every person who, by or through stock ownership, agency, or  
15 otherwise, or who, pursuant to or in connection with an agreement or  
16 understanding with one or more other persons by or through stock  
17 ownership, agency, or otherwise, controls any person liable under  
18 sections 77k or 77l of this title, shall also be liable jointly and  
19 severally with and to the same extent as such controlled person to any  
20 person to whom such controlled person is liable, unless the  
21 controlling person had no knowledge of or reasonable ground to  
22 believe in the existence of the facts by reason of which the liability of  
23 the controlled person is alleged to exist.

24 Id. “To state a claim under this section, a plaintiff must allege that the . . .  
25 defendants had power or influence over the company and that the . . . defendants

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26 <sup>18</sup> Insofar as Defendants’ argument is related to “standing,” In re Westinghouse  
27 states that this concern is better addressed during the class certification stage in the  
28 proceedings. See In re Westinghouse, 90 F.3d at 718 n. 22. See also Danis v. USN  
Communications, Inc., 189 F.R.D. 391, 400 (N.D. Ill. 1999) (addressing argument at class  
certification stage).

1 were culpable participants in the company's alleged illegal activity." In re Daou,  
2 397 F.3d at 725. Bain contends that it is not a "controlling person" because it  
3 meets neither of these requirements. The court disagrees.<sup>19</sup>

4 First, the Prospectus itself indicates that Bain "had power or influence over"  
5 DDi at the time that DDi issued the Prospectus. In particular, the Prospectus  
6 provided:

7 Our current principal stockholders will continue to have significant  
8 influence over our business after this offering . . . . Upon completion  
9 of this offering, . . . investment funds affiliated with Bain Capital, Inc.  
10 will beneficially own approximately 14.2% of our outstanding  
11 common stock. In addition, of the eight directors who serve on our  
12 board, three are current representatives of Bain Capital, Inc. and two  
13 are former representatives of Bain Capital, Inc. By virtue of such  
14 stock ownership and board representation, these entities will continue  
15 to have a significant influence over all matters submitted to our  
stockholders, including the election of our directors, and to exercise  
significant control over our business, policies and affairs.

16 Prospectus at 12. See also id. at 66 ("Five of our directors are or were affiliated  
17 with our principal stockholder, the Bain Capital funds."); id. at 68 (Bain held  
18 20.4% of DDi common stock before Offering). Given the liberal pleading  
19 standard imposed by Rule 8(a), this statement in the Prospectus is sufficient at this  
20 stage in the proceedings to demonstrate that Bain "had power or influence over"  
21

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22 <sup>19</sup> The defendants named in this claim also argue that they cannot be held liable  
23 under § 15(a) because DDi, the allegedly "controlled" entity, is not named in this suit.  
24 The court need not address this argument because it was raised for the first time in  
25 Defendants' reply briefs. See In re Intuit Privacy Litig., 138 F. Supp. 2d 1272, 1275 n. 3  
26 (C.D. Cal. 2001) ("this court does not consider arguments raised anew for the first  
27 time in a reply brief as to so do would unfairly deny the non-moving party an opportunity  
28 to respond"). Defendants additionally argue that they cannot be held liable under § 15(a)  
because there is no underlying violation of § 11 or § 12. This argument fails, as certain  
portions of Plaintiffs' § 11 and § 12 claims survive the instant motions to dismiss.

DDi at the time the Prospectus was issued. Cf. No. 84 Employer-Teamster Joint Council Pension Trust Fund v. America West Holding Corp., 320 F.3d 920, 945 (9th Cir. 2003) (“Whether [the defendant] is a controlling person is an intensely factual question . . .”).

Second, Plaintiffs have alleged that Bain was a “culpable participant” in the alleged wrongful conduct. For example, Plaintiffs allege that Bain “control[led] the contents of the . . . Prospectus,” but did not “ma[ke] a reasonable investigation or possess[] reasonable grounds for the belief that the statements contained in the . . . Prospectus were true and devoid of any omissions of material fact.” SAC ¶¶ 111, 113. Given Rule 8(a)’s liberal pleading standard, this allegation is sufficient. Thus, Plaintiffs have adequately alleged that Bain was a “controlling person” under § 15(a).

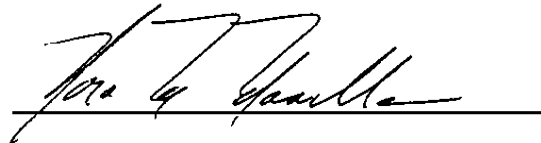
## V. CONCLUSION

For the foregoing reasons, Defendants’ motions to dismiss are **GRANTED** in part and **DENIED** in part. First, Plaintiffs’ claims asserted on behalf of those who purchased the Convertible Notes are time-barred and are dismissed with prejudice. Second, Defendants’ motions to dismiss Plaintiffs’ § 11 claim asserted on behalf of those who purchased DDi common stock pursuant to or traceable to the Prospectus are denied. Third, Defendants’ motions to dismiss Plaintiffs’ § 12(a)(2) claim insofar as it is asserted on behalf of those who purchased DDi common stock in private or secondary market offerings are granted; this portion of Plaintiff’s § 12(a)(2) claim is dismissed with prejudice. Fourth, Defendants’ motions to dismiss Plaintiffs’ § 12(a)(2) claim against Bain and the Individual Defendants are granted; this portion of Plaintiff’s § 12(a)(2) claim is dismissed without prejudice. Fifth, the Underwriter Defendants’ motion to dismiss Plaintiffs’ § 12(a)(2) claim against them is denied. Sixth, Defendants’ motions to dismiss Plaintiff’s § 15(a) claim are denied.

1 No later than August 8, 2005, Plaintiffs shall file either an amended  
2 complaint or a notice confirming that the SAC will remain the operative  
3 complaint. If Plaintiffs choose the latter course of action, Defendants shall file an  
4 answer by August 29, 2005.

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6 IT IS SO ORDERED.

7 DATED: July 20, 2005

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10 Nora M. Manella  
11 United States District Judge  
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